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May 13, 2008

AGENDA ITEM 3d

TO: MEMBERS OF THE BENEFITS AND PROGRAM ADMINISTRATION COMMITTEE

I. SUBJECT: AB 2940 (De Leon)—As Amended April 10, 2008

California Employee Savings Program

Sponsor: The New America Foundation

II. PROGRAM: Legislation

III. RECOMMENDATION: Neutral, if Amended

While the Board supports policies that enhance supplemental savings plans as a means to encourage savings for retirement, there are potential risks associated with this bill.

IV. ANALYSIS:

AB 2940 would establish the California Employee Savings Program ("Program") to be administered by the California Public Employees' Retirement System ("CalPERS"). Specifically, this bill would require CalPERS to offer one or more individual retirement accounts or individual retirement annuities (collectively "IRAs") to California employees of a participating private-sector or non-profit employer. The IRAs offered under the Program may include traditional IRAs, payroll deduction IRAs, SIMPLE IRAs, or other IRAs authorized under Section 408 and 408A of the Internal Revenue Code (the "Code").

Background

Individual Retirement Accounts (IRAs)

Traditional IRAs – include tax-deferred retirement savings accounts whereby taxes are not paid on contributions and investment earnings until withdrawal, and ROTH IRAs, where contributions are made on an after-tax basis and are not subject to taxes upon withdrawal. These IRAs are available whether or not an individual is covered by another retirement plan, however, the income tax

deductibility of their contributions may be affected if they or their spouse is covered by an employer retirement plan. The contribution limit is \$5000 for 2008. This is the maximum that can be contributed in 2008 regardless of whether the contributions are to one or more traditional IRAs or whether all or parts of the contributions are nondeductible. A traditional IRA is not sponsored by an employer so the assets are not considered pension plan assets subject to the Employee Retirement Income Security Act of 1974 ("ERISA"), nor are the contributions made through payroll deductions.

Payroll Deduction IRAs – are for employers who do not want to adopt a retirement plan, but still want to allow their employees to save through payroll deductions. The decisions about how much to contribute up to the \$5000 limit, and when to contribute are made by the employee. Although the limits and the contributions to a payroll deduction IRA are tax-deductible to the same extent as traditional IRAs, it provides a more convenient and consistent means for the employee to make these contributions. Depending upon how the payroll deduction IRA is set up and level of endorsement by the employer, the IRA assets may be subject to ERISA.

Savings Incentive Match Plans for Employees of Small Employers, or SIMPLE IRAs – are a savings option for employers with 100 or fewer employees that allow employees to contribute a percentage of their salary each pay check and to have their employer contribute too. Under a SIMPLE IRA, employees can contribute up to \$10,500 annually. Employers can either match up to 3 percent of an employee's wage or make a fixed contribution. SIMPLE IRAs are considered pension plan assets and are subject to ERISA.

Simplified Employee Pensions, or SEP IRAs – allow employers to set up an IRA for their employees. Employers are required to contribute a uniform percentage of pay for each employee, but they are not required to make contributions each year. An employer may contribute up to 25 percent of an employee's compensation up to the annual cap, which is \$45,000 in 2008 and subject to annual cost-of-living adjustments for later years. SEP IRAs are considered pension plan assets and are subject to ERISA.

CalPERS' Management of Supplemental Income Plans

CalPERS' Supplemental Income Plans Division currently administers three deferred compensation (DC) plans designed to provide supplemental retirement income to public employees. The first DC plan is a 457 governmental plan ("CalPERS 457 Plan") that is available to employees of all California local public agencies, county superintendents of school offices, and school and community college districts that elect to contract for it. Currently, over 600 participating public agencies contract with CalPERS to offer the CalPERS 457 Plan to allow their employees to voluntarily invest a portion of their salary among their choice of nine separate Core Investment Funds and eight asset allocation funds. The CalPERS 457 Plan investments and services feature no hidden fees or restrictions. Total fees for administration and asset management of the Core

Investment Funds are less than 1 percent. The CalPERS 457 Plan also offers a Self-Managed Account option that allows participants to invest in over 4,000 mutual funds at the regular retail rate through a discount brokerage service. CalPERS uses one of the leading administrators of private retirement plans and mutual funds in the industry, State Street Corporation and its affiliates, CitiStreet, State Street Global Advisors, and State Street Brokerage, to assist with administration, record keeping, and customer service.

In addition to the CalPERS 457 Plan, the Supplemental Income Plans Division also administers the Supplemental Contributions Program (SCP), which is an after-tax money purchase pension plan under section 401(a) of the Code that is available to state employee members of CalPERS, as well as employees of public agencies and schools that contract for the SCP. The third DC plan administered by CalPERS is the State Peace Officers' and Firefighters' (POFF) Plan, which is also a money purchase pension plan under IRC 401(a), that receives specified employer contributions for members of certain collective bargaining units in state service.

ScholarShare College Savings 529 Program

The State Treasurer's Office ("STO") oversees the ScholarShare College Savings 529 Program, and contracts with Fidelity Investments for administration of the plan, including investment selection and management (mutual funds), recordkeeping, custody, enrollment, marketing and customer service. The role of the STO is limited to marketing the program to both individuals and employers, monitoring performance and performing oversight. Some employers permit payroll deductions for employees who participate in the 529 Program.

The ScholarShare Program's internal annual operating budget is \$2.4 million for 7 positions, which is primarily funded through a 10 basis point fee assessment. Fidelity Investments also recoups its costs through investment management fees. The STO implemented the ScholarShare Program in 1999 with a \$5 million loan from the State, which was amortized over an 8 year period and paid off last year. Given the similarities between ScholarShare and the Program created by AB 2940, the start-up and operational costs of the Program could be expected to be similar, after accounting for inflation.

One of the keys to the success of having 529 College Savings Programs run and sponsored by individual states is that their proponents were able to pass federal legislation and obtain regulatory approvals before approval and implementation at the state level.

EDD Payroll Tax Program Operations and Capabilities

The Employment Development Department (EDD) supports state activities and benefit programs by collecting and administering employment-related tax programs, including Unemployment Insurance (UI), Disability Insurance (DI), Employment Training (ET), and Personal Income Tax (PIT) Programs. Similar to

the administrative structure of CalPERS' defined benefit programs EDD separates the employer reporting and contribution collecting functions of these programs, from their benefit determination and payment functions. EDD's Tax Branch is responsible for the former function, and is one of the largest tax collection agencies in the nation. It handles all administrative, education, customer service, and enforcement functions for the audit and collection of UI and ET from taxes on employers, and withholding of DI and PIT from employees. Each year, EDD collects more than \$31 billion in payroll taxes, including nearly \$25 billion in PIT, processes more than 30 million employer payroll tax documents and remittances, and maintains records for more than 17 million workers.

Universal Retirement Savings Proposals in Other States

Retirement savings proposals similar to AB 2940 have recently been introduced or considered in a number of other states, including Connecticut, Maryland, Michigan, Vermont, and Washington. None of these proposals have been signed into law.

Maryland – The Legislature recently considered and rejected Senate Bill 728, which would have established the Maryland Voluntary Employee Accounts Program (MVEAP) administered by the Maryland Teachers and State Employees Supplemental Retirement Plans. Authorized plan structures under the MVEAP would have included 401(a) plans, including 401(k) plans, as well as trusts or savings incentive match plans under 408(p) of the Code. Instead, and at the Legislature's instruction, the Maryland Supplemental Retirement Plans recently conducted a study of Voluntary Employee Accounts to examine cost efficiencies, potential for state liability, and organization and administration requirement with regard to a state-sponsored program.

The study concluded that each participating businesses would have to routinely and regularly sign and return documents to a central administrator, provide annual reconciliation of contribution history, and follow instructions on distribution and collection of miscellaneous employee communication materials. It estimated that the MVEAP would require a subsidy of between \$300,000 and \$500,000 a year for at least five to seven years. Estimated costs included: design and drafting of special plan documents that describe the structure of the accounts, specific control mechanisms, and specific employer responsibilities; draft, submit and obtain rulings from the IRS and Department of Labor that approve plan documents with an estimated duration of 12 to 18 months.

Washington – The Legislature has considered five universal retirement savings proposals since 2003. Last year, it appropriated money for the Washington Department of Retirement Systems (DRS) to produce a report scheduled for release this December, which studies the various legal issues and obstacles that must be addressed in order to implement such a plan. The current legislative vehicle is House Bill 2044, which would create the Washington Voluntary Accounts Program (WVAP) to offer employees a vehicle for saving and private

employers a method for offering benefits. The bill designates the State Treasurer as the custodian of the WVAP account, and allows the DRS to implement and operate the WVAP either in-house or through an external third party contract. It also makes implementation and operation contingent on funding and allows the DRS to freeze or reduce enrollments and establish a waiting list if continued enrollment would cause expenditures to exceed revenues.

Vermont – HB 70 expands participation in 457 and 403(b) deferred compensation plans the State offers to its own employees to nonprofit corporations or other employers authorized by the IRC to participate in such DC programs.

Michigan – SB 24 would allow small business employees to participate in a newly established 401(a) pension plan administered by the Michigan State Department of Management and Budget.

Connecticut – SB 652 is a one paragraph measure that requires the State Controller to establish a tax-qualified defined contribution retirement program to provide retirement investment plans to self-employed individuals, small employers with no more than 100 employees, and non-profit organizations. The Controller is authorized to contract with a third-party administrator to manage the plans, and recover implementation and operating costs from plan assets.

Proposed Changes

Specifically, this bill would:

- Establish the Program to be administered by CalPERS for California employees of participating private-sector or non-profit employers.
- Require CalPERS to offer one or more IRAs under the Program, including traditional IRAs, payroll deduction IRAs, SIMPLE IRAs, or other IRAs authorized under Sections 408 and 408A of the Code
- Authorize CalPERS to employ staff and retain or contract with financial institutions, investment managers, consultants, administrators and other service providers.
- Allow CalPERS, in its discretion, to select from among several possible structures and/or features of the IRAs offered under the Program.
- Allow employers to participate in the Program and make contributions to their employees' IRA accounts.
- Allow participating employers to automatically enroll their employees into the Program.

- Require employers that do not participate in the Program to allow individual employees who elect to participate to designate a portion of their wages to be forwarded to the Program.
- Require CalPERS to provide cost-effective assistance to participating employers and employees to facilitate compliance of the IRAs offered under the Program with the Code, including tax qualification, or, where applicable, ERISA, or any other legal or accounting requirements.
- Require CalPERS to market the Program to employers and employees, and provide retirement education services to participants.
- Require CalPERS to utilize pooling and standardization of investments to provide economies of scale, to the extent allowed under federal law.
- Require CalPERS to be reimbursed for Program expenses from participants' contributions, and Program assets and investment returns, except for expenditures that are provided for through a State appropriation. Although the bill provides that the Legislature may make an appropriation for the implementation and administration of the Program, it does not contain an appropriation at this time
- Specify that the exemptions in law provided to public retirement plans shall not apply to the implementation and administration of the Program.
- Require CalPERS, as a condition of implementing the Program, to seek all necessary approvals, rulings, determinations, etc. from federal entities, including the Internal Revenue Service ("IRS"), the United States Department of Labor ("DOL"), and the Securities Exchange Commission ("SEC"), to ensure the plans and IRAs established under the Program adhere to all federal requirements regulating the operation of retirement plans and the offering, sale, or distribution of securities under those plans.
- Provide that no claims, tax liens, etc. by the state, its agencies or instrumentalities may apply against any IRA accounts or Program funds or assets.
- Indemnify the Board, CalPERS employees and contracting investment managers for acts related to the implementation and administration of the Program.
- Require EDD to implement and maintain a payroll deduction program necessary to implement the Program.
- Require CalPERS to submit progress and status reports to the Legislature and to participating employers and individuals.

- Allow CalPERS to defer execution of the Program until it has obtained all approvals it deems necessary for its implementation.

Legislative History

- 2008 AB 2123 (Liu) a companion measure to AB 2940 by the same sponsor, - would establish the California Financial Literacy Initiative to be administered by the State Controller: 1) authorizes the Controller to make financial literacy information available online and via toll-free telephone in English, Spanish, Chinese, Tagalong, Vietnamese, and Korean; 2) authorizes the Controller to convene a Financial Literacy Advisory Committee with representatives from state agencies, financial institutions, and nonprofit agencies; 3) requires the Controller, as resources are available, to establish and oversee the California Financial Services Corporation, to provide financial information to low-and moderate income Californian's. The Corporation would be staffed by volunteers with professional certifications in financial planning or comparable training; and 4) establishes the California Financial Literacy Fund in the State Treasury to accept donations from nonprofit entities to be appropriated by the Legislature to support the purposes of the Initiative. *CalPERS' Position: None.*
- 1997 Chapter 851 (AB 530, Committee on Higher Education) – Established the Golden State Scholarshare Trust Act, administered by the Student Aid Commission, as a structured open savings program for individuals and families to pay future costs of higher education, including public and private colleges, universities and vocational institutions. *CalPERS' Position: None.*
- 1990 Chapter 1659 (SB 2026, Craven) – Authorized CalPERS to offer a 457 plan, 403(b) plan, or any other form of deferred compensation arrangement authorized by the Internal Revenue Code and approved by the CalPERS Board. The bill requires the program be self-funded through fees assessed against participating employees and/or contracting employers and invested in a series of accounts set-up within the new Public Employees' Deferred Compensation Fund. *CalPERS' Position: Support*

Issues

1. Arguments by Those in Support

According to the Author, the California Employee Savings Program will offer secure, voluntary and portable individual retirement savings accounts that workers can freely take from job to job without penalty, providing them with the opportunity to build their assets and help prepare them for their retirement, at no cost to taxpayers.”

Organizations In Support: New America Foundation (Sponsor); Advanced Composite Products and Technology; California ACORN; California Small

Business Association; Fraser Communications; Green Apple Books; Greenlining Institute; Kuschel & Company, LLC; Lerner + Associates Architects; Morris and Garritano Insurance; R6 Interiors; Sacramento Asian Pacific Chamber of Commerce; San Francisco Council of District Merchants Associations; San Francisco Chamber of Commerce; San Francisco Small Business Advocates; Sfrent.net; SF Works; Small Business California; Small Business Majority; Small Business Network; Tree Lovers Floors, Inc.; Wallace Remodeling, Inc.; WCBS.

2. Arguments by Those in Opposition

The opponents applaud the Legislature for considering initiatives to increase retirement plan coverage but have concerns about establishing a state-run system. Instead, the opponents believe that making people aware of existing private sector options is both more cost-efficient and effective and state agencies and state legislators can play a helpful role in efforts to expand coverage by increasing public awareness about the retirement plan options that are already available to small employers as well as federal tax incentives that minimize start-up costs for employers who offer retirement plans.

Organizations in Opposition: Retired Public Employees' Association; Securities Industry and Financial Markets Association.

3. Plan Structure Considerations

AB 2940 would allow CalPERS to administer the Program through various structures that could limit its direct involvement in the management and fiduciary decisions that employers and qualified retirement plan providers generally make. Most of the bill's requirements can be met through contracts with private-sector service providers, with management and oversight provided by CalPERS' professional staff.

In effect, AB 2940 would allow the Board to determine CalPERS' level of involvement in the operations of the Program, from developing and administering the Program completely in-house, to contracting-out all these functions to a third party, or a combination of the two approaches. The legal issues and respective risks will depend upon how the Program is ultimately structured and implemented. The more discretionary control CalPERS has over the Program (i.e. serves as trustee, asset management) the greater the potential legal issues and risks.

4. Plan Design Considerations

The intent of AB 2940 appears to focus on increasing retirement savings among the lower-paid and more mobile sectors of the California workforce. A portion of this task is to improve financial awareness and education to these potential savers, which is the focus of a companion measure mentioned earlier, AB 2123 (Liu). Another part of the effort involves creating a retirement

savings vehicle tailored to the needs of these potential savers with simple to understand, low cost, stable investment products that provide a reasonable rate of return. However, this effort must be balanced by the need to ensure affected employers are willing to undertake the additional administrative responsibilities and legal liabilities necessary to provide such tax-advantaged retirement savings plans. This difficult balance is achieved through an exhaustive plan design process to research participant behavior, explore administrative structures to increase efficiencies, and compare investment options and strategies.

Because AB 2940 requires the Program to be self-sustaining, the IRAs must maintain administrative costs at a level that participants are willing to bear through fees charged either as a percentage of assets in their accounts, or through a fixed annual fee. The highest administrative costs for plan providers are typically those associated with participant enrollment, recordkeeping, termination and distributions, therefore, it may be necessary to restrict eligibility for enrollment until participants have been employed by an employer for a certain period. An alternative approach is to require higher initial contribution amounts to increase likelihood that administrative costs associated with establishing and closing individual accounts can be recovered from participants.

Another consideration is when participants are allowed to make contributions that are too small, the administrative costs of the plan may consume a large percentage of their assets, which tends to discourage participation or encourage cost-shifting. It may be necessary to specify minimum contribution amounts to increase the likelihood that participants are able to enjoy adequate return on their investment after administrative and investment costs are deducted from their accounts. Other common plan design considerations that have an effect on expenses and participation include: terms and conditions of vesting for employer contributions; fixed contributions rates or a range of choices, choice of default investments, terms and conditions of participant access to their retirement savings; and the ability to limit or cease enrollment based on market conditions in order to ensure the solvency of the Program.

5. Plan Offering Considerations

CalPERS is a governmental plan as defined under Section 3(32) of ERISA and, as such, it is exempt from ERISA coverage. This bill would require CalPERS to offer one or more various types of IRAs (see Background Section), most of which are likely subject to ERISA. Offering traditional IRAs maintained by individuals should not give rise to ERISA coverage. On the other hand, SIMPLE IRAs, SEP IRAs, or other employer-sponsored plans would be subject to ERISA. Payroll deduction IRAs fall somewhere in the middle. CalPERS would need to work with the United States Department of Labor ("DOL") to make sure that any such payroll deduction IRAs would be exempt from ERISA before offering them under the Program.

Although the Program may be administered through various means, with different features and structures, CalPERS would need to consider whether the IRA assets could be effectively walled off to prevent ERISA creep to the non-ERISA assets managed by CalPERS. If CalPERS lost its governmental plan exemption, CalPERS would be subject to additional responsibilities, duties, and stringent reporting and disclosure requirements under ERISA. CalPERS would also be subject to the jurisdiction of the United States Department of Labor ("DOL") and potential participant lawsuits.

6. Program Start-Up Funding Considerations

The CalPERS defined benefit plan is a pension plan qualified under Section 401(a) of the Internal Revenue Code (IRC) and, as such, assets of the PERF may only be used for the exclusive benefit of the employees or the beneficiaries of the employers sponsoring the plan. This "exclusive benefit rule" prohibits the use of PERF assets to fund the start-up costs and on-going expenses of the proposed Program. To avoid violating this "exclusive benefit" rule, AB 2940 must specify another funding source such as the General Fund, and appropriate money over several years until the Program cannot only become self-sustaining, but also generate sufficient excess revenues to repay these "loans". The Legislature may wish to consider providing an initial General Fund appropriation that would not be subject to repayment to cover all or a portion of the Program start-up costs, especially CalPERS' expenses associated with obtaining the approvals and/or exemptions necessary for its implementation and promotional costs to establish public consciousness of the Program.

7. Investment Considerations

Because a portion of current employer and employee contributions are able to cover all existing benefit payments to CalPERS members and their beneficiaries, CalPERS is able to hold investments in the Public Employees Retirement Fund ("PERF") for long periods of time, whether they be equity, real estate or other asset types. Other CalPERS-managed funds and benefit programs such as the POFF Plan and the Public Employees' Long Term Care Fund do not have similar actuarial experience and liquidity requirements, and consequently, these funds hold fewer asset classes and have different investment strategies. As a result, these other funds do not experience the same rates of investment return as the PERF rate.

Another major difference between most CalPERS-managed funds and IRAs is that CalPERS funds collectively serve hundreds of thousands of participants and are operated under the assumption they will never be terminated, while an IRA only lasts the lifetime of a single participant. This requires a different investment strategy and asset allocation as participants move through the accumulation phase during their working careers, when asset growth is emphasized, to the distribution phase in retirement, when asset protection becomes more important.

8. Federal Regulatory Considerations

Commingling Assets

There are some limitations on commingling retirement assets with other types of assets. These rules limit the ability to offer a “group trust” type of investment to individuals and non-governmental plan investors. The actual structure used will need to be carefully reviewed for commingling issues.

IRS Approval of Non-Bank Trustees

Existing federal law requires the trustee or custodian holding IRA assets to be a bank, federally insured credit union, savings and loan association, or entity approved by the IRS to act as a trustee or custodian. Because CalPERS does not meet any of these definitions, it would be necessary to seek additional IRS approval, or contract with a third-party administrator or trustee that satisfies this requirement.

Securities Issues

The federal securities laws generally contain exclusions for state entities and their officers and employees from all provisions of the Investment Company Act of 1940, the Investment Advisers Act of 1940, and the Securities Exchange Act of 1934. Currently, CalPERS as a governmental entity is exempt from these regulatory structures. When creating the administrative structure of the Program, careful consideration should be given to whether the activity performed by CalPERS under the Program would subject it to these securities laws.

9. Additional Legal Considerations

Fiduciary Issues

Federal and state law require retirement plan assets to be held in trust for the exclusive benefit of retirement plan participants and beneficiaries. Article XVI, Section 17 of the California Constitution grants the CalPERS Board of Administration (“Board”) with plenary authority and fiduciary responsibility for investment of moneys and administration of the California Public Employees’ Retirement System (“CalPERS or System”). The Board has a constitutional duty to administer the System in accordance with its fiduciary responsibility for investment of the moneys and administration of the pension system. The Board must discharge its duties with respect to the pension system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable administrative expenses. The California Constitution specifies that the Board’s duty to participants and their beneficiaries shall take precedence over any other duty.

Under AB 2940, the Board would also be charged with administering the Program for employees of participating private-sector employers. If the Board has a legal duty to administer the Program established under AB 2940 and all of CalPERS benefit programs, including its pension, health, and long-term care plans, this may present potential conflicts of interests between the interests of the CalPERS public pension plans and the plans administered under the Program.

Constitutional Issues

Article XVI, Section 17 of the California Constitution generally prohibits the State from loaning its credit for subscribing to, or otherwise having an interest in the stock of any company, association, or corporation. This prohibition, however, does not apply to a retirement board of a “public pension or retirement system.” As used in subdivision (h) of this Section, the term “retirement board” means the board of a “public employees’ pension or retirement system.”

It is not clear whether this exemption would extend to the Board’s administration of the Program since it would expand coverage to private-sector employees, as opposed to public employees. This may become an issue depending on how the Program is structured. For example, if CalPERS were to offer its internally managed funds as “side-by-side” funds to the participants of the Program, CalPERS would have an interest in stock. Because the exemption to the constitutional prohibition only extends to a retirement board of a public employees’ pension or retirement system, this exemption would not likely extend to participants under the Program. Accordingly, a constitutional amendment might be necessary if the Program included CalPERS internally managed funds.

10. Automatic IRA Act of 2007

In this Congressional session, H.R. 2167 and S.1141 were introduced to allow employees not covered by qualified retirement plans to save for retirement through automatic payroll deposit IRAs, and provide the self-employed with similar arrangements. Employers would be required to allow employees to make a payroll-deduction deposit into IRAs. Although these proposals do not appear to have progressed, these bills could be an appropriate vehicle to address the regulatory issues raised in this analysis. It may be prudent to wait for the passage of federal legislation before a state-sponsored program is created.

11. Alternative Approaches to Meet the Proposal’s Intent

Placing the administration of this Program with another state agency would eliminate a number of the legal issues and risks associated with administering a private-sector retirement savings plan through a public retirement system. State agencies with related expertise include the Department of Personnel

Administration (which administers the State SavingsPlus Program that includes the 401(k) plan and the 457 deferred compensation plan for state employees), the Controller, the Treasurer (which administers the ScholarShare Program), or numerous existing state finance boards. This approach is illustrated in the recent legislative proposal in Connecticut which would require the State Controller solicit, select and oversee a third-party administrator to provide a model 401(k) plan to small employers.

12. Legislative Policy Standards

CalPERS' Legislative Policy Standards suggest a neutral position or no position for proposals that have conflicting policy implications. Among these significant considerations, the Board must balance its support of policies that enhance supplemental savings plans as a means to encourage participants to save for retirement and supplement their defined benefit pensions, with its opposition to policies that potentially threaten the Trust. Therefore, staff recommends that the Board adopt a NEUTRAL, if amended, position on AB 2940.

This bill should be amended to: (1) provide an adequate State appropriation to cover start-up costs and account for the Program's "ramp-up" period; (2) require approval from the federal regulatory bodies, including the DOL, the SEC, and the IRS, that the IRAs or plans offered under the Program would maintain exemptions to the same extent as "governmental" plans; and (3) other minor clarifying amendments.

V. STRATEGIC PLAN:

This item is not a specific product of the Annual or Strategic Plans, but is a part of the regular and ongoing workload of the Office of Governmental Affairs.

VI. RESULTS/COSTS:

Program Cost

Although, the intent of AB 2940 is for the Program to be self-funded and have the costs fully covered by fees deducted from the participants' IRA contributions, it would be necessary for the State to appropriate or loan funds to CalPERS and EDD to cover its start-up costs. EDD's start-up costs are unknown, but expected to be substantial. CalPERS start-up costs are outlined below.

In addition, AB 2940 would provide indemnity to the Board from the State General Fund for any claim or loss sustained by reason of any decision or action related to the administration of the Program. The potential liability from this Program is real, so this creates a potential litigation expense for the State.

Administrative Costs

CalPERS' costs for developing, administering, and marketing the Program can be divided into two phases: (1) initial development and start-up costs; and (2) ongoing administration or operating costs. The estimated start-up costs would be approximately \$1.74 million for 13.2 PYs over an implementation period of approximately 18 to 30 months. This amount includes approximately \$500,000 in one-time costs associated with securing the services of outside tax and securities counsel to, among other things, assist CalPERS in obtaining the necessary federal regulatory approvals. Once the Program was developed and became operational, CalPERS' ongoing administrative costs would range from \$806,000 to \$1.46 million annually, for 7.7 to 15.4 PYs. This figure does not include advertising costs. Both the start-up and operational costs of CalPERS would require an appropriation until the Program is self-sustaining. Continuing annual appropriations may be required for an indefinite period pending the build-up of assets sufficient to generate fee revenues off-setting CalPERS' annual operational costs. This appropriation, however, would not include costs incurred by EDD.

CalPERS could conduct a formal request for proposal ("RFP") to select a third-party administrator, trustee, and investment provider. Costs and expenses charged by the service provider would be determined based on the scope of work and the bids submitted. These fees would be assessed in addition to the costs incurred by CalPERS itself. While it is anticipated by the bill's sponsor that administrative costs would be recovered through the fees charged participants, this would depend upon on the level of participation and the amount of assets in the Program.

While reporting through the EDD as envisioned in AB 2940 may streamline procedures for participating employers, the cost of Program administration borne by participating employees may actually be higher by reporting payroll through the EDD system, as additional liability and plan compliance risks might be implicated. This determination cannot be made until EDD is able to provide an estimate of its projected costs under the provisions of AB 2940.

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